CHAPTER 6: TELECOMMUNICATIONS IN TEXAS – PAST, PRESENT, AND FUTURE

As in previous years, this Scope of Competition Report has focused on competition in wireline voice services. In most of the past reports, local competition could only be discussed in terms of niche providers, with long distance services being the main arena of competition. With the implementation of PURA 95 and the FTA finally underway, the 1999 Scope Report could finally document a CLEC presence in the local telecommunications market. In the last Scope of Competition Report, in 1999, the evidence could support only what can perhaps be called a "toe-hold" for competition.

Evidence available for this report clearly demonstrates that competitive providers have a visible market share, with dozens of CLECs entering the more lucrative local wireline voice markets in Texas by the end of 1999. Clearly, the potential exists for creating competition in local telephony in the urban areas of Texas, if not the state as a whole.

Though trends of the last several years suggest that Texas is poised for competition in local voice telephony, events in the year 2000 have created a dramatically different backdrop for competition in local voice telephony. The recent slump in the share prices of CLECs and the reorganizations of AT&T, Sprint, and Worldcom announced in the fall of 2000 suggest that CLECs may be heading for a period of consolidation

In the next five years, however, even more sweeping changes in technology and the newly found ability of the former monopolies and CLECs to offer "one stop shopping" for a wide range of telecommunications services will overshadow the fight for market share in wireline telephony. Future reports may focus on these trends far more than on the entry of CLECs into the local wireline service territories of Verizon, SWBT, and Valor.

Past: CLECs Flood into Texas

There exists in Texas a legal and regulatory framework that can facilitate competition to enter local telephony for customers of SWBT, Verizon, and Valor Telecommunications (the ILEC in some of Verizon's former service territories). The Commission opened the door to competition in wireline for SWBT through SWBT's Section 271 proceeding, arbitrations between SWBT and CLECs, and various rulemakings.

In 1998 and 1999, in response to these new opportunities for entry into local voice telephony, CLECs entered the Texas market as rapidly as anywhere else in the United States. A recent FCC study on competition for local voice service found that Texas ties New York for being the states with the largest number of operating CLECs. This result, on its face, supports the notion that the regulatory atmosphere in Texas is friendly for competition.

Such factors as population growth, economic growth, and population density also appear to be important considerations in the decisions of CLECs to invest in or resell voice telephony facilities in a given area of Texas. The Large Metropolitan areas and the Suburban counties, which combined comprise almost 60 percent of Texas' population, have heavy concentrations of CLECs. Data show that the Dallas and Houston metro areas have about twenty or more CLECs serving customers, while San Antonio and Austin have ten or more CLECs serving customers. Many rural areas that allow for customer choice have a choice of two, three, or more CLECs, in addition to an ILEC. Some of these competitors, however, may be aimed at customers with poor credit histories and are not vying for the average local customer's business.

Data for 1999 show while statewide CLECs are using equally all three means of entry that the FTA envisioned – construction of new lines, purchase of UNEs, and resale of telephone service - to gain entry into local telephony, the strategy varies dramatically by size of the market. CLECs built facilities in Dallas, Houston, San Antonio, and Austin to compete with ILECs, particularly for business customers. Outside the Large Metro areas, however, CLECs pursued customers by purchasing UNEs and reselling telephone services.

The market share of local access lines of CLEC in the Suburbs is about 12 percent and in Large Metropolitan areas about eight percent. The eight percent figure probably masks a wide range of market penetration rates that includes a lower penetration rate in El Paso and higher penetration rates in the Dallas and Houston, areas. The latter have large and growing residential and business populations, a high population density, and high *per capita* incomes. Seventy percent of CLECs' customers in the Large Metro areas and Suburbs are businesses.

CLECs in rural areas are showing little or no market share at this point, but that fact may reflect in part the legal and regulatory prohibitions to competition as well as poor economics of doing business in rural areas. (Counties with a population of 20,000 people or fewer have a CLEC penetration rate of less than 2 percent.) Seventy percent of their customers are residential. The entry of some telephone cooperatives into the market, particularly those in or near wealthier parts of West Texas, may indicate that some CLECs might be focusing on rural or small-town areas that allow customer choice. These CLECs may possess expertise that can make them very competitive without drawing competition from companies with deep pockets.

Having CLECs enter new markets is only the first stage of offering customer choice. CLECs must have the power to fight for market share for a sustained period before Texans harvest the fruits of competition. A key factor in developing competition in local telephony over time will be the capitalization of those CLECs.

The good news for the 1998-1999 period was that about a quarter of CLECs had market capitalizations of at least $1 billion, an order of magnitude comparable to the capitalizations of the two largest ILECs, Verizon and SWBT. Areas of Texas served by these well-capitalized CLECs were much better positioned to receive the benefits of competition in local telephony and the benefits of competition for bundled services ("one-stop shopping").

Though almost 100 CLECs responded to the Commission survey, two-thirds of the CLECs were private firms with capitalizations that were unknown or less than $100 million. These CLECs may have limited prospects that may lead to failures and mergers for many of them under the best of market conditions.

Affiliates of eight cooperatives have filed as CLECs, located near areas with high *per capita* incomes. Given that most of them have small capitalizations of $20 million or less, it will be a formidable task for them to become more than regional or niche players. Rural areas where ILECs face their primary competition from these CLECs face uncertain prospects for competition in local telephony in the long term.

Present: ILECs Adapt, CLECs Struggle

ILECs

The ILECs that must allow the greatest customer choice – SWBT and Verizon – responded to new market opportunities in 1998 and 1999. Indirect effects of deregulation and competition in local exchange service in Texas have led to a sale of rural exchanges in Texas in 1999-2000. Verizon and SWBT have contended with the heavy investment in facilities by CLECs in the metropolitan areas of Texas. With competition increasing in some parts of their service territories, these companies had incentives to rethink their holdings and strategic approach to selling telephony in Texas.

Southwestern Bell

SWBT's competitive position in Texas has strengthened considerably in the past year. SB 560 granted SWBT pricing flexibility in vertical services, an important means to lower prices where competition with CLECs exists, and raise prices where competition is limited. For example, in 2000 SWBT significantly increased the prices for a number of nonbasic services, often services that are very popular and for which competitive alternatives are limited.

SB 560 also granted SWBT the ability to competitively bundle its products. An important additional piece in SWBT's "one-stop" shopping strategy was SWBT's receiving a favorable recommendation from the Commission on its Section 271 application, leading to FCC approval for SWBT to offer long distance service in Texas in the second half of 2000. SWBT at present has very limited competition in providing bundled services in Texas.

Verizon

During the last two years Verizon implemented an additional strategy to cope with shareholder or market pressure, including reducing its presence in local voice markets in Texas as a CLEC. Verizon chose to sell some of its rural exchanges in various states to earn a better return on its assets in a changing telecommunications industry. Verizon's sale of a number of rural exchanges to Valor this year was part of this national trend.

A number of ILECs across the country have been seeking changes in the geographical boundaries of their operations to meet competitive challenges elsewhere. According to a recent U.S. General Accounting Office (GAO) survey of state public utility commissions, of the nearly 832,000 access lines that major ILECs have sold from January 1996 through April 2000, an estimated 68 percent were in rural areas.[106] The GAO analyzed 27 pending sales, totaling 901,000 access lines, and found that 872,000, or 97 percent, were in rural areas.

Telephone cooperatives and small private telephone companies in rural parts of Texas might do something similar to the Verizon sale and merge or purchase each other's service territories. These ILECs could then capture economies of scale and use their expertise in handling the multitude of services and would possess sufficient capitalization to invest in lines and equipment to upgrade a system in the targeted service territory. The quality and range of services, therefore, might improve in parts of rural Texas even without direct competition from CLECs, competition that is very unlikely until alternative technologies described in this report become widely available.

CLECs

In the second half of the 1990s, technological breakthroughs and deregulation in the telecommunications industry created new and highly uncertain investment opportunities for investors. By the late 1990s, investors in the telecommunications industry faced investments that had a high risk / high reward profile in an industry that was once considered the realm for retirees searching for a safe, fixed return on assets. Venture capitalists, private investors, and commercial banks flooded the telecommunications industry with investment capital.

As a result, in the late 1990s, the telecommunications industry saw a proliferation of small or poorly capitalized CLECs that were vulnerable to the level of risk investors (mutual fund managers, investment banks, and commercial banks) would tolerate over time. Large long-distance carriers such as AT&T and Worldcom made large-scale investments in new technologies to compete with SWBT for customers that wanted "one-stop" shopping in telecommunications services.

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[106] United States General Accounting Office, *Telecommunications: Issues Related to Local Telephone Service*, Report to the Ranking Minority Member, Committee on Commerce, Science, and Transportation, U.S. Senate, GAO/RCED-00-237 at 5 (August 2000).

The rush into the new world of telephony created a classic bubble in telecommunications stocks.[107] According to a NASDAQ index of telecommunications companies, share prices rose 300 percent from January 1998 to early March 2000. By early 2000 such an increase provided CLECs with large capitalizations, allowing them to challenge ILECs for market share in local exchange service in Texas.

As with other stock market bubbles, this one burst, forcing the industry to endure bankruptcies of some leading CLECs and massive restructuring of others. Increased competition by ILECs in long distance, and the perception by the market that long-distance service using dedicated switched circuits was yesterday's technology, took its toll on the three dominant long distance carriers. Some analysts believe that traditional long-distance business is going away and will be replaced by any-distance calls and data transmissions that also include voice.[108] With the entry or potential entry of ILECs into long-distance telephony, prices and revenues for long-distance providers have fallen, contributing to the fall in the market capitalization of large CLECs.

The fall in the market capitalizations of large CLECs that are long distance carriers has left them in a weaker position to provide competition in local exchanges in Texas. In October and November 2000, these long-distance carriers announced their intentions to reduce their emphasis on residential services in Texas as part of massive restructuring of their business lines.

The sharp fall in share and bond prices in 2000 for CLECs may presage consolidation in the telecommunications sector. A handful of CLECs that each had capitalizations of $1 billion or more in 1999 saw their share prices drop over 95 percent during 2000. Thirty-eight of the CLECs that responded to the data collection instrument stated that they had not started serving customers in Texas at the end of 1999 and may not have sufficient revenue to weather the decline in the financial support needed to challenge an ILEC.

By the end of 2000, SWBT's financial position had strengthened relative to the CLECs. SWBT's entry into the long distance market has weakened the ability of CLECs to challenge SWBT in local voice service. Without investor confidence and funding, in the near term CLECs might pose a weaker challenge to SWBT for local wireline voice telephony or in the "one-stop" shopping market than they did in 1998 and 1999. The Commission has noted that in 2000 SWBT raised its prices on a number of vertical services and was successful in rapidly gaining market share in the long distance market, even though it was offering interLATA long distance to only customers who had SWBT as an ILEC.

In the short term, the largest potential impact of CLECs' financial troubles will be to limit their ability to enter a local market by making long-term investments in plant and equipment. Physical investment in new plant and equipment is the most powerful means to develop competition in local wireline telephony, allowing CLECs to own an increasing

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[107] For a description of how stock market bubbles have inflated and burst over the past three centuries, see Charles Kindleberger, *Manias, Panics, and Crashes*, Wiley Investment Classics, Fourth Edition, 2000.

[108] For a detailed discussion of this point, *see* J.P. Morgan Securities, Equity Research, *Telecom Services*, "A Fresh Look at the Industry" (Sept. 8, 2000).

share of the local exchange infrastructure relative to the ILECs while expanding wireline capacity in a local market overall.

Future: Technology Spawns Competition

While short-term disruptions in the financing of CLECs may slow the advance of competition in wireline telephony, the long-term prospects for competition in telephony look promising. Disruptive new technologies, the rise of the Internet Protocol as an increasing backbone to telecommunications, and deregulation are massively restructuring the telecommunications industry. A result of all these changes is a massive increase in telecommunications services and products that will be available to customers, along with a decreasing emphasis on wireline voice telephony.

Projections that telecommunications industry analysts at J. P. Morgan Securities made in September 2000 can provide a sense of the magnitude of these changes that may occur in the next five years, as shown in Table 27. J.P. Morgan Securities projects that revenues in telecommunications services nationwide will grow from $246 billion in 1999 to $422 billion in 2005. Wireline voice (local and long distance) revenues are expected to decline slightly between 1999 through 2005. As a percentage of total revenues, however, local wireline voice will fall from 33 percent in 1999 to 21 percent in 2005, and long distance wireline voice will fall from 32 percent in 1999 to 16 percent in 2005. In contrast, data services' share of total telecommunications revenues will rise from 12 percent in 1999 to 21 percent in 2005, and the Internet's share of total telecommunications revenues will rise from 4 percent in 1999 to 16 percent in 2005.

Table 27 – Forecast of Revenues in the Telecommunications Industry

	1999		2005E	
Service	$ in Billions	Percent of Total	$ in Billions	Percent of Total
Local Voice	87.8	33.0	92.6	20.8
Long Distance Voice	84.0	31.6	71.1	16.0
Wireless	40.0	15.1	100.1	22.5
Internet	10.5	4.0	69.7	15.7
Data Services	31.4	11.8	90.8	20.5
Other ILEC	11.9	4.5	19.8	4.5
Total	265.5	100.0	444.1	100.0

Source: J. P. Morgan Securities, *Telecom Services Industry Analysis*, September 8, 2000.

One trend influencing the direction of the industry is the rise of the Internet Protocol for delivering voice and data to customers. While Voice over Internet Protocol is not currently a viable alternative for local telephony, the indirect effects of this revolution are profound on telecommunications providers. Industry giants such as AT&T and SWBT are reorganizing business lines and altering their emphasis towards data and Internet services. Many analysts who follow the telecommunications industry believe that voice telephony likely will become more of a commodity business, no longer sold as a separate service.

Another trend that will affect competitive delivery of voice telephony will be the alternatives to wireline discussed in Chapter 4. Growth in satellite, cable, and wireless services to customers will change the market structure of local telephone service by providing several means to deliver local telephone service. The locations where alternative providers offer these services would affect the level of competition across different areas of Texas. The number of CLECs on wireline in a rural area may not be as important as the opportunity for area customers to have several portals. In areas that currently have numerous CLECs on wireline, the competition will be even fiercer but not fully captured in the data of regulated telecommunications providers.

Competition Outlook

The Commission has implemented the Texas Legislature's framework for deregulating local voice service in Texas. As a result, CLECs have entered the Texas market in the past two years and have provided competition in certain regions of Texas.

The market for business customers in the Large Metro areas of Texas appears to be competitive. Facilities-based competition has provided increased capacity for CLECs to compete with ILECs over the long term. Monopoly power exists, however, in residential and rural markets in Texas. Key CLECs that were expected to challenge SWBT are now limiting their push into residential voice markets in Texas.

The Commission recognizes that differences in personal income and population density among various regions of Texas also affect where CLECs decide to compete for residential customers. At the same time, however, cross-subsidies that have traditionally kept residential rates artificially low have contributed to the lack of competition for residential customers.

The Commission believes that long term re-regulation of residential and rural markets should not be necessary, as new technologies could dislodge the monopolistic position of ILECs in certain areas of Texas in coming years.

CHAPTER 7: LEGISLATIVE RECOMMENDATIONS

1. TAKE FURTHER STEPS TO FACILITATE LOCAL EXCHANGE COMPETITION IN TEXAS

The *2001 Scope of Competition Report* summarizes the path taken to open century-old monopolies as well as the use of new tools for facilitating competition that the Texas Legislature provided last session. As detailed above, the response has been good in some markets and disappointing in others. The conclusion today is that competition looks viable in the business and urban markets, but may not be as viable for certain rural and residential customers. The *Report* offers an economic diagnosis for why this pattern has developed, with the primary causes rooted in underlying market conditions and in the historical regulatory pricing system for local telephone service.

Texas has had a long-standing public policy to provide universal service and to maintain low rates for basic residential local service. However, continuing this policy means that some segments of the market may not receive rates that reflect the true cost of the service. In the short term, these segments - most notably residential and rural customers - may need protection from price increases if the market does not effectively moderate them. Indeed, further action may be necessary to ensure that competition comes to these markets at all. The Commission recognizes that short-term remedies are not long-term solutions in regulating a telecommunications industry that is rapidly evolving away from selling simple voice service.

There are a number of ways Texas can go from here. Approaches can be passive or active. The Commission suggests that the Legislature consider at least the following options for addressing the lack of competition in Texas local residential and rural markets:

Option A: Passive Erosion (no change to current pricing structures).

This is the de facto policy now in effect. If the market is left to behave freely under current policies, residential customers will continue to have low rates for basic service, but incumbent carriers likely will raise rates further on nonbasic services with little competition under the pricing flexibility granted in SB 560. The economic term for the process of aligning rates to reflect actual costs is called rebalancing. A benefit of allowing these rates to rise is that higher rates for the total set of residential services (even with basic service rates held artificially low) would provide CLECs incentives to offer competitive bundled service packages and to bring new technologies to more areas of Texas. As a result, CLECs may be able to erode the market share of incumbents over the long term.

However, a likely consequence of this approach is that CLECs will serve profitable high-end residential customers and the remaining customers, especially low-end residential and rural customers, may experience price increases for commonly used services for which there are no affordable substitutes at this time. So, while the bundled price of residential telephone services will move closer to its true cost, the burden of rebalancing prices would continue to be borne by the vertical services user, while basic local services remain subsidized below true cost. From the public's point-of-view, this arrangement may be preferable to having that burden be borne by all residential dial-tone customers.

Option B: Place a temporary, two-year price cap on popular nonbasic residential services that do not currently have competition, and evaluate whether further steps are necessary at the close of the cap to ensure competition in these markets.

This option borrows from both laissez-faire and regulatory economics. Placing caps on residential call forwarding, caller ID, and call return, - the prices of which have increased substantially since SB 560 became effective - would moderate the burden borne by residential customers during the transition to competition for local exchange markets.

Most residential and rural customers receive basic local services at rates well below their true cost (with the remainder of the cost subsidized by Texas and federal universal service payments and over-priced vertical or nonbasic services). The best hope many of these customers have for competition is from alternate technologies – such as wireless, satellite, or cable – that are not yet cost-competitive with landline basic local service. Landline local exchange competitors may never be competitive with incumbent-provided basic local service at current, subsidized rates. Therefore, the primary benefit of price caps on nonbasic services would be to temporarily protect residential customers from further price increases for services that have already seen large price increases. Such a strategy would allow the opportunity to see if the bundled local service package is priced high enough to allow more competitors to serve more residential and rural customers.

A disadvantage of this approach is that competitive providers need sufficient profit to fight for and win market share from incumbent carriers. Caps on vertical services will also affect competitors' profits slowing innovation in telephony services. At the present time, the Commission has observed that incumbent carriers are often charging prices for nonbasic services that are 5 to 10 times higher than their costs and, in some cases, 100 times higher than their costs. Capping prices at these levels would not limit opportunities for competitors to enter the market profitably.

Option C: Authorize and direct the Commission to hold a proceeding to rebalance costs into a structure that gives competitive providers the incentive to compete in residential and rural markets.

Most residential customers get a majority of their basic local services below cost. Rebalancing of rates would establish residential and rural rates that more closely, reflect the true costs of service. CLECs would have greater incentives to enter new markets in Texas with a wider range of sophisticated services for customers outside the large metro areas. Higher, rebalanced local rates would give local service providers much more economic headroom to deploy advanced telecommunications technologies and services for rural and residential customers.

This approach, however, has several drawbacks. After years of subsidized low rates, many customers would face increases in basic service rates as a result of rate rebalancing. Determining the proper, cost-based price for basic service in a given area would be difficult. Raising the rates for basic local services to meet costs might not permit competition anyway, as lower income and sparsely populated areas of Texas may never be profitable enough to attract competitors in traditional local service for reasons other than retail pricing.

Option D: Combine Options B and C

Combine Options B and C for a comprehensive solution that includes the short-term protection of price caps and the long-term incentives of rebalancing prices to more fully reflect costs. The advantage of this approach is that any negatives associated with the moratorium on certain residential service prices under Option B can be evaluated and adjusted in the course of rate rebalancing. Furthermore, such a proceeding and its implementation are likely to take most of the two years of the Option B moratorium. The cap on prices may mollify negative public reactions that otherwise could result from higher prices, while allowing residential and rural customers to reap the benefits of a wider range of telephone services in the future.

While one of these approaches may be desirable, the Commission believes that long-term re-regulation of residential and rural markets should not be necessary. While monopoly power is still a factor in residential and rural markets at this time, new technologies appear to have the potential to stimulate vigorous competition in a number of parts of Texas in the years to come. Until then, the Legislature's price cap on traditional phone services serves as an appropriate customer protection.

2. *Facilitate Access to Flat-Rate Local Dial-Tone Service for Texans in Uncertificated Service Areas*

Currently, numerous potential customers for local exchange telephone service do not have access to reliable, flat-rate dial-tone and other features of local exchange service because they are located in uncertificated service areas in Texas. Uncertificated service areas are areas where no telecommunications provider is obligated to provide telephone service. While all electric utility customers in Texas are served by at least one electric utility company, customers located in areas totaling approximately 10,000 square miles in Texas have no telecommunications provider obligated to provide access to dial-tone. This situation was created when the original service areas were established and no incumbent local service provider wanted to serve these rural and sparely populated areas. Following a twenty-five year period of growth, these previously uninhabited rural areas are becoming more populous.

The Commission regularly receives requests from residents in uncertificated areas to obtain dial-tone. Commission staff members have encountered instances of telecommunications providers refusing to connect potential customers to the network, even if the customer builds a line up to the provider's demarcation point. In addition to lacking access to reliable dial-tone service and emergency 9-1-1 service, these potential customers lack access to Internet service providers and advanced services. Because telecommunications providers are not currently required to serve uncertificated areas, Texas citizens are denied access to reliable, flat-rate dial-tone service, emergency 9-1-1 service, and the Internet. The only communications options that Texas citizens are afforded in uncertificated service areas are BETRS (radio), cellular, and satellite communications services. Even these options can be severely limited due to geographic dead spots in the coverage.

The Commission recommends that the Legislature consider the following two options for bringing reliable dial-tone to Texans located in uncertificated areas.

(1) Authorize the Commission to assign each uncertificated area in Texas to a telecommunications provider with the understanding that funding from the Texas Universal Service Fund (TUSF) would be available for the recovery of certain costs associated with the provision of dial-tone in uncertificated areas. The Commission notes that the optimal means for providing dial-tone to a particular area may depend upon a variety of geographic, economic, technological, and other area-specific factors. Accordingly, assignment of this service extension would be made on a technology-neutral basis. Similarly, TUSF funding for the recovery of certain costs associated with providing dial-tone to the customer also would be considered regardless of the technology used to provide this service.

(2) Give the Commission the responsibility to evaluate requests for dial-tone from persons located in uncertificated areas and to authorize the Commission to require a telecommunications provider to provide dial-tone to a prospective customer, on a case-by-case basis. Again, the optimal means for providing dial-tone to a particular customer may depend upon a variety of factors best determined within the scope of each request. Consequently, the assignment and funding of this service extension would be made on a technology-neutral basis.

The Commission remains committed to a system of telecommunications in Texas that does not exclude citizens on the basis of location. If it is the intent of the Legislature to provide all Texans with access to reliable local exchange telephone service, including dial-tone, the Commission encourages adoption of one of these two options.

3. Clarify and Ensure Commission Authority to Protect Proprietary Information

As deregulation is implemented, telecommunications providers and potential new entrants have more concerns about competitively sensitive information. Recent judicial decisions and legislative revisions have left governmental bodies without the independent legal grounds necessary to seek protection of commercially sensitive information received from third parties. This inability to assure providers that such information will be protected from disclosure has hampered the Commission's ability to complete legislatively mandated reporting duties, such as the regular scope of competition reports and this year's reports on advanced services and switched access.

In the utility industry in Texas, the Legislature has carefully scripted the move from monopolies in the provision of telecommunications and electric services to competitive markets. It has also given the PUC duties, such as providing a scope of competition report, that require that the PUC be given access to commercially sensitive information in order that it might provide well-educated guidance on the movement of the market to competition. In the newly competitive market, the PUC has become the hunting ground for competitors to find commercially sensitive information about their competition. Without the ability to gather and protect commercially sensitive information, the PUC becomes a thorn in the side of competition.

As noted several times in Chapters 3 and 4 of this *Scope Report*, the Commission was either unable to gather the data it needed to prepare the *Scope Report*, or unable to gather it in the most useful format. Many entities expressed concern that the Commission could not protect the information once it became an agency document due to the recent change in Tex. Gov't Code § 552.110, and the Attorney General's letter ruling in OR2000-344 (February 2, 2000).[109]

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[109] Prior to the 76th Legislative session, Section 552.110 of the Texas Government Code allowed governmental bodies to protect commercial information obtained from third parties if the information was privileged or confidential by statute or judicial decision. In deciding whether such third-party information was excepted from disclosure under § 552.110, the Attorney General applied the two-prong test set out in *National Parks Conservation Ass'n v. Morton*, 498 F.2d 765 (D.C. Circuit 1974). DM-ORD 639 (1996). *National Parks* allowed governmental bodies to protect third-party commercial or financial information if disclosure would be likely to impair the government's ability to obtain necessary information in the future, or would cause substantial harm to the competitive position of the person from whom the information was obtained.

In a later D.C. Circuit case, *Critical Mass Energy Project v. Nuclear Regulatory Commission*, 975 F.2d 871 (D.C. Circuit 1992) *cert. denied*, 507 U.S. 984 (1993), the court found that the *National Parks* two-prong test should apply only to commercial or financial information that third parties are required to file with governmental bodies. The court further found that information submitted voluntarily should only be excepted from disclosure if the information is of a kind that the provider would not customarily make available to the public, under 5 U.S.C. § 552(b)(4). *Critical Mass II*, 880.

In 1999, the Austin Court of Appeals effectively overruled the application of the *National Parks* test in DM-639 (1996) when it found that *National Parks* is not a judicial decision within the meaning of the [former] § 552.110, Gov't Code. *Birnbaum v. Alliance of Am. Insurers*, 994 S.W.2d (Tex App.–Austin 1999, pet. denied). Thus, under the current Texas Public Information Act, § 552.110, financial and commercial information would not excepted from disclosure by applying the *National Parks* test alone.

By SB 1851 in the 76th Regular Legislative Session, the Legislature revised § 552.110 to cure in part the void left by the *Birnbaum* decision. The revised § 552.110 does not address the governmental body's inability to obtain information from third parties that those parties deem commercially sensitive. The Commission has run head long into the void left by this combination of judicial decisions and legislative action.

To mitigate this problem, the commission seeks revision of § 552.110 of the Texas Government Code to provide governmental bodies with an independent ground for asserting the exception for commercially sensitive information. In particular, § 552.110 should be revised to allow a governmental body to protect third-party information from disclosure *if* disclosure is likely to impair the governmental body's ability to obtain necessary information in the future *and* if the information is not customarily released to the public by the person from whom it was obtained.

An exemption for governmental bodies to protect commercial material is justified in that it protects the rights of those who are required to provide commercially sensitive information to a governmental body and it encourages cooperation from those entities that are not required to provide the information. By revising § 552.110 as suggested, governmental bodies will have a basis to assert an exception for not disclosing information that it has received from third parties, whether voluntarily or not. The burden will first be on the governmental body to prove that it needs the information and that the third party does not customarily make the information available to the public.

The aggregated data that the Commission used as the basis for Chapter 3 was a blunt but sufficient instrument for the purposes of this current *Report*. These purposes were primarily to identify broad competitive trends in basic local services in the infancy of competition, where competitive providers focused on serving business customers in four metro areas in Texas. However, as the market in local basic service evolves in the next five years the Commission will need more refined data to better understand the dynamics of competition in Texas. Having access to a more complete set of data in future scope of competition reports will help the Commission better understand the Texas market. As a result, the Commission will be able to identify and implement better practices and provide more specific recommendations to the Legislature concerning the dynamics of competition in local service.

The Commission can identify a number of examples of where the data collection instrument would be insufficient for analysis in future Scope Reports. Staff needs the ability to change the data groupings to reflect the findings of its research. For example, regional analysis of competitive providers can yield an important insight into the extent of competition. For data confidentiality reasons in this report, the Commission allowed data to be aggregated for urban regions of a certain population size, which allowed the following cities into the same category: Austin, Dallas, El Paso, Houston, and San Antonio. Unfortunately, staff subsequently determined from other sources that competitive providers did not enter El Paso as aggressively as they did the other four cities, but staff could not regroup the data to put the four cities in a new category and assign El Paso into a more appropriate group.

Further, the Commission needs the ability to analyze individual counties and the competitive providers operating therein. For instance, when staff discovered that a number of coops in west Texas filed to become competitive providers, it consulted survey data, which showed that competitive retailers had gained a larger market share in the Texas Panhandle than in other rural areas of Texas. Staff suspected that some of these coops were winning market share in the Texas Panhandle, but, without direct access to the data, Staff could not determine which coops were winning market share. With that knowledge, staff could have, on a confidential basis, interviewed these providers to better understand how the Commission could promote competition in rural areas of Texas.

The Commission also could not calculate the common market share index known as the HHI on the basis of data collected through the Commission's data request. Large IXCs were not willing to let the ILECs report to the Commission information on originating minutes of use, which was needed to calculate an HHI for intrastate long distance. Commission staff finally obtained the information from the biggest ILECs (but not the others), but only after much persistence, involving coordination with both those ILECs and the big IXCs.

Information needed by the Commission to conduct industry analyses and to provide a full picture of the utility markets in Texas can only be obtained from utility companies, some of which are no longer regulated entities. The Commission has no authority to require certain entities, like municipal power companies, to provide data to the commission, but the Commission nonetheless needs the data in order to fulfill its statutory duties. Accordingly, § 552.110 should be revised as noted above to give the PUC and other governmental bodies an independent ground upon which to base a request for an exception to disclosure for information that has been provided a governmental body, whether voluntarily or involuntarily.

4. Clarify that Telecommunications Providers have Burden of Proof in Slamming and Cramming Complaints

In contested cases concerning slamming complaints, the Commission has encountered disputes as to whether and how a utility must demonstrate that it has complied with PURA and Commission rules for authorizing a change in a customer's preferred carrier.

The Commission recommends that PURA be clarified to require that a telecommunications utility initiating a switch in the customer's preferred carrier be required to demonstrate that it complied with the provisions in PURA and commission rules in order to refute any allegation of slamming (unauthorized switch) or of cramming (unauthorized charges).

Such clarification regarding slamming could be made in PURA by adding language such as the following to PURA § 55.309.

- Upon a showing that a telecommunications utility has failed to respond or provide proof of verification in accordance with the requirements in this Subchapter and commission rules, the burden of proof shall be on the telecommunications utility initiating a switch in a customer's preferred telecommunications utility to provide clear and convincing evidence that the switch was authorized in accordance with such requirements.

Adding he following language to PURA § 17.159 could achieve a similar result with respect to cramming.

- Upon a showing that a telecommunications utility has failed to respond or provide proof of verification in accordance with the requirements in this

Subchapter and commission rules, the burden of proof shall be on the telecommunications utility imposing the charges for a product or service to provide clear and convincing evidence that the charges were authorized in accordance with such requirements.

5. Grant 9-1-1 Commission Sufficient Authority to Accomplish its Mission

The inability of the Commission on State Emergency Communications (CSEC or the 9-1-1 Commission) to manage and control deadlines for the installation and testing of equipment between the local telephone companies and wireless carriers has delayed the availability of advanced emergency capabilities offered by enhanced 9-1-1 (E911) systems.

The 76th Texas Legislature passed H.B. 1983, which gave the CSEC the responsibility for implementing wireless Phase I 9-1-1 services for at least 75% of the population served by the State program. This implementation was to be completed on or before August 31, 2000. CSEC did not meet this deadline.

Specifically, CSEC encountered problems getting certain ILECs, CLECs, and wireless companies to place and fulfill trunk orders and to begin and complete the testing and implementation process necessary to complete Phase I service. CSEC does not have the necessary jurisdiction over the telecommunications carriers to require compliance with the Phase I requirements. CSEC must rely on the Commission and the FCC for enforcement purposes.

Although the Commission worked closely with CSEC to help with deployment of Phase I in Texas, the implementation is still not complete. Specifically, the Commission worked with regulated carriers to ensure that trunks ordered by wireless carriers were installed and tested to meet the deadline set by HB 1983. As a result, wireless Phase I 9-1-1 service was deployed in Texas covering 80.6% of the population served by the state program, as of December 14, 2000.

Under Phase I, 9-1-1 systems must deliver the phone number of the handset from which an emergency call originates and the location of the base station carrying the call to the 9-1-1 operator. Under Phase II, 9-1-1 systems must locate handsets within a radius of 125 meters with a success rate of 67 percent. The requirements for Phase II do not take effect until October 1, 2001.

In order to assist CSEC in completing its Phase I and Phase II wireless implementation projects, the Commission recommends that the Legislature grant CSEC limited jurisdiction over ILECs, CLECs, and wireless telecommunications providers. This limited jurisdiction would include enforcement powers to assess administrative penalties in order ensure full compliance in the Phase I and Phase II 9-1-1 wireless implementation projects and other 911-related projects and activities in the future.

Other Commission Recommendations

In other legislatively mandated reports, the Commission has discussed and made the following recommendations:

Advanced Services Report Recommendations

1. Recommended Objectives for Public Policy

Establish a goal that all Texans have access to advanced services by a date certain to meet policy goals set in state and federal legislation

Encourage deployment of advanced services to rural Texans in a technology neutral manner for cost-effectiveness

Avoid Excessive and Intrusive Regulation

Encourage Local Solutions

Avoid "One Size Fits All" Solutions

2. Specific Policy Alternatives to Encourage Deployment

Expand Data Collection Activities

Implement Demand Aggregation

Implement Anchor Tenancy

Encourage Community Networks

Provide Community Internet Access And Training To "At Risk" Populations

Use Economic Development Funds for Rural Telecommunications Infrastructure Investment

Provide Tax Incentives for Deployment

Deploy Fiber Optic Cables in the State's Rights of Way

Allow Private Access in Limited Situations to the TEX-AN 2000 Infrastructure

Provide Narrow Exception for Rural Municipal Governments to Provide Advanced Services

Enhance Statewide Telecommunications Strategic Planning

SWITCHED ACCESS REPORT RECOMMENDATIONS

Provide the statutory ability for the Commission to restructure access charges and reduce access charge revenues for Chapter 58 and 59 ILECs

Authorize the Commission to hold a combined proceeding, rather than separate ones for each company, to restructure and reduce access charges for small incumbent local companies and cooperatives

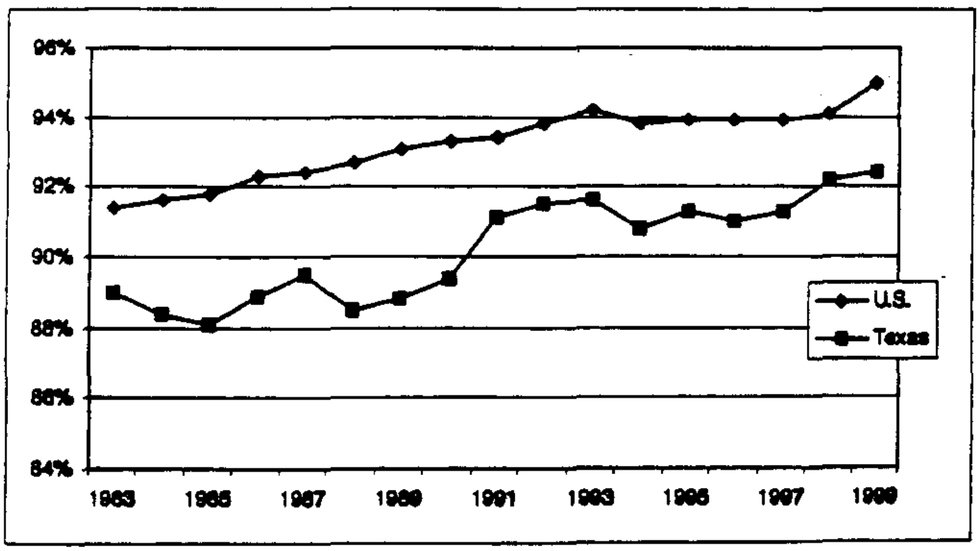
Extend the expiration date of PURA Section 52.112 in order to ensure corresponding customer protections resulting from switched access charge reductions

APPENDIX A: UNIVERSAL SERVICE

One of the primary historical goals of telecommunications regulation has been to ensure universal service, *i.e.*, that all customers have access to affordable telecommunications service. Section 254 of the federal Telecommunications Act of 1996 (FTA) contains provisions designed to ensure universal service within the environment of competitive local telephone service. The FCC names universal service as one of the three pillars of the FTA trilogy for competition.

A measure of the success of universal service support programs is the overall subscribership to telephone service. The FCC, with the assistance of the U.S. Census Bureau, monitors the percentage of households with telephone service, as reflected on the chart below. While Texas remains below the national average, our state continues to show improvement in subscribership.

Figure 15 – Percentage of Households With a Telephone



Universal Service Programs in Texas

The 70th Texas Legislature established a Universal Service Funding (USF) mechanism for Texas through amendments to PURA in 1987. Statutory changes were made to the Texas USF programs in subsequent years. The current Texas USF program is described in Chapter 56 of PURA, and consists of the following major components:

- Support for targeted lifeline services (such as Tel-Assistance),
- Support for a telecommunications relay service for the hearing- or speech-impaired (Relay Texas),
- Support for the specialized telecommunications assistance program,
- Support for the provision of high-capacity (T-1) services to certain entities (*e.g.*, educational institutions, libraries, and others), and
- Support for the provision of basic telecommunications service in high cost rural areas.

Table A-1: Texas' Universal Service Fund Program Disbursements

USF Program Disbursements	FY 1999 (Actual)	FY 2000 (Actual)	FY 2001 (Estimated)
High Cost Fund – Non-Rural Telcos	0	383,546,184	442,467,500
High Cost Fund – Small Rural Telcos	38,084,091	94,087,265	99,257,517
Small Telco Recovery - PURA §56.025	2,965,448	4,448,171	4,448,172
Lifeline and Tel-Assistance Programs	2,487,056	11,653,838	12,136,601
Reduced Rate T-1s for Certain Entities	0	739,599	838,100
Relay Texas Program	6,816,004	10,007,130	10,609,650
Specialized Telecom Assistance Program	322,420	578,402	716,171

High-Cost Support

In January 2000, the Texas PUC formally implemented revisions to the Texas High Cost Universal Service Plan (THCUSP) portion of the Texas Universal Service Fund. The THCUSP provides support to eligible telecommunications providers that serve the high cost rural areas of the state. Two separate mechanisms are used: one for non-rural carriers, and another for small and rural ILECs.

The program for non-rural carriers provides that the THCUSP will support basic local telecommunications service provided by an eligible carrier in a high cost rural area that is carried over all flat-rate residential lines and the first five flat rate single-line business lines at a business customer's location. Under the rule, support is competitively neutral; therefore, support for a customer location is portable across providers. Generally, the amount of support available to each eligible carrier is based on a comparison of the forward-looking economic cost (calculated using a cost proxy model) to specific revenue benchmarks. To avoid a windfall as a result of implementation of the THCUSP, the PUC's rules require equivalent rate reductions.

The PUC recognized that state and federal statutes place small and rural carriers on a different competitive footing than other carriers, and therefore established a separate mechanism to enable the small and rural carriers to prepare for the advent of competition in local telephony and the transition to the THCUSP. Specifically, the PUC's rules establish guidelines for determining per-line support amounts for each study area, ensuring the provision of basic local telecommunications service at reasonable rates in a competitively neutral manner in those areas of the state. Monthly per-line support for each eligible small/rural carrier consists of the sum of (1) the amount necessary to replace support previously provided by the intraLATA toll pool and (2) the loss of revenue realized by the carrier upon implementing Commission-ordered switched access and intraLATA toll rate reductions.

In addition to the THCUSP, several small ILECs are eligible for support under PURA § 56.025. This portion of the USF was designed to ensure recovery of revenues that resulted from regulatory actions prior to 1998, and also to compensate carriers for other revenue shortfalls resulting from regulatory actions.

Tel-Assistance and Lifeline Service

Tel-Assistance Service is a telecommunications service assistance program that provides low-income residential customers with a reduction in the price of their basic local exchange service. Eligible customers receive a 65% reduction in their applicable basic monthly local exchange service rate. The Texas Legislature created this program in 1987, and it is codified in PURA §§56.071-56.079. As of October 2000 there were 42,612 households receiving Tel-Assistance support. The amount of revenue support received from the Texas USF by companies providing Tel-Assistance discounts was $2,925,587 for the fiscal year ending in August 2000.

All ILECs in Texas and any CLEC receiving TUSF now offer Lifeline Service. Lifeline Service allows eligible residential customers to receive a total discount on their monthly local exchange service rate of $11.35. The discount is funded through Federal USF and Texas USF support. More than 209,230 households in Texas receive monthly Lifeline Service discounts. The Texas USF revenue support for Lifeline Service was $8,728,251 for the fiscal year ending in August 2000.

In addition to monthly support, Link-Up Service, an adjunct federal program to Lifeline Service, provides a partial waiver of non-recurring residential installation charges for local service up to $30.00. Link-Up Service support is included in the figure for Lifeline Service support shown above.

As a result of interstate and intrastate merger agreements, SWBT and Verizon will be initiating supplemental Lifeline Service support programs in 2001 for a 36-month duration. SWBT's Lifeline USA and Verizon's Alternative Lifeline Service will provide eligible residential customers with a complete waiver of local service installation fees. Both programs incorporate public outreach, including commercial advertisements, in an effort to increase eligible participants' opportunities to connect new telephone service.

Relay Texas Program

In 1989, the Legislature authorized a telecommunications relay service (TRS) in Texas and directed the Commission to supervise its provision.[110] The name "Relay Texas" was coined for the Texas TRS. Relay Texas is available 24 hours a day, 365 days a year, with no restrictions on the length or number of calls placed. In September 1990, the first month of operation, Relay Texas processed nearly 50,000 relay calls; by September 2000, the number of calls had increased to an average of over 415,000 per month. Relay Texas has led the nation in improving the quality of TRS, with such enhancements as voice-carry-over, speech-to-speech, Texas Video Interpreting Service, a customer database, Spanish interpreting, and other new features. Pursuant to PURA, TRS is provided by a designated carrier and funded by a surcharge on all telecommunication providers through the USF. Using a request-for-proposal process, the Commission selects a vendor based on such key criteria as price, service quality, and availability over a five-year term. The Commission awarded five-year contracts to Sprint Communications Company, L.P. (Sprint) for Texas in 1990 and in 1995. Sprint has again been selected as the preferred vendor, and the new contract is under negotiation. The new contract will expire in 2005.

A model for competition in the provision of TRS is difficult to discern, but interest in creating a competitive market in this area has increased. AT&T, Sprint, and Hamilton provide the vast majority of TRS at both the state and national level, although there are several other smaller telephone companies providing TRS in a few states. Based on experience thus far, it is unclear whether the TRS market in any one state can support multiple TRS providers. California experimented with TRS multi-vendoring by releasing a Request for Proposals with the understanding that whichever proposer had the lowest bid would be allowed use of the existing 800 relay numbers. Other qualified TRS providers were welcome to provide TRS in California, provided that they too billed at the same low bid price. MCI was awarded the California 800 TRS numbers. AT&T refused to offer TRS, arguing that the price per minute was too low. Sprint countered with a proposal for California to combine all the prices and use the average bid price. California agreed and Sprint participated. Last month, MCI advised authorities that it could no longer provide service at the current price, and offered a non-negotiable price per minute. California rejected MCI's offer. Sprint also proposed a new, higher price per minute, which is still under consideration.

In the past, the five-year contract term used by the Commission limited the ability of Texas TRS to keep up with technological advances because the incumbent vendor had no incentive to offer a competitive price. In 1999, the Texas Legislature passed a bill amending the Relay bill by allowing the Commission to seek other vendors for special features of the relay service if the incumbent provider is unable to provide the feature at the best value for the state. This amendment has helped to ensure that special services can be sought at a competitive price from another TRS provider if the incumbent TRS provider is not able to offer a reasonable price.

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[110] Now codified in PURA §§ 56.101-112.

Specialized Telecommunications Assistance Program (STAP)

A new program initiated by the Texas Legislature in 1997 was created to provide financial assistance to persons with disabilities to purchase special telecommunications equipment. The new program, called the Specialized Telecommunications Assistance Program (STAP), is coordinated by two agencies: the Texas Commission for the Deaf and Hard-of-Hearing (TCDHH) and the PUC. The PUC is responsible for registering and reimbursing vendors from the TUSF. TCDHH is responsible for the bulk of operations, from developing applications, to approving equipment, to issuing vouchers. Texas uses a voucher system under which qualified persons pay a $35 application fee and receive a voucher to purchase the telecommunications equipment. Unlike in many other states, the equipment becomes the property – and responsibility – of the purchaser. Approved products, such as TTYs, amplified phones, speech aids, and video software, assist persons with a wide variety of disabilities in using the telephone, some for the very first time. More than 5,700 telecommunications vouchers have been issued to persons with disabilities since the inception of the STAP in 1998.

Federal Universal Service Programs

One of the primary purposes of universal service support is to allow ILECs and other eligible telecommunications carriers to provide certain basic services to customers in high-cost areas without having to charge these customers unaffordable rates. Historically, in the interest of meeting the goal of universal service, ILEC services have been supported or subsidized to enable high-cost consumers to be served at rates that are reasonably comparable to those in lower cost areas. This universal service support has been both explicit and implicit.

Explicit Support. Several federal programs have provided explicit universal service support in the form of direct monetary payments to carriers. This support has been provided for both intrastate and interstate services. For example, the FCC's high-cost support mechanism provides support for the costs of the intrastate portion of the local loop that significantly exceed the national average. By providing this federal support for intrastate costs, the FCC assists the states in ensuring that rates for intrastate rates remain affordable and reasonably comparable.

Implicit Support. In addition to receiving explicit universal service support, ILECs also received implicit universal service support from a variety of sources. Some rate structures have permitted ILECs to charge rates for certain services that significantly exceeded the costs of providing those services, thereby enabling those ILECs to charge below-cost rates for other services. For example, the practice of averaging rates over large geographic areas, for both intrastate and interstate services, results in subscribers in low-cost areas subsidizing the rates of subscribers in higher cost areas.

This "patchwork quilt" of implicit support helped keep rates largely affordable in a monopoly environment, where ILECs could be guaranteed an opportunity to earn returns from certain services and customers that are sufficient to support the high cost of providing other services to other customers. The new competitive environment envisioned by the FTA, however, threatens to undermine this implicit support structure.

The FTA removed barriers to entry in the local market, generating competitive pressures that may make it difficult for ILECs to maintain charges above economic cost.

Recognizing the disruptive effects that competition would have on universal-service support mechanisms developed in a monopoly environment, Congress instructed the FCC, after consultation with the Federal-State Joint Board on Universal Service (Joint Board), to establish specific, predictable, and sufficient mechanisms to preserve and advance universal service. Congress concluded that the support provided by these mechanisms "should be explicit and sufficient to achieve the purposes" of section 254, which include the purpose that all Americans should have access to telecommunications services at affordable and reasonably comparable rates. In response to this directive, the FCC has taken several actions to put universal-service support mechanisms in place that will be sustainable in an increasingly competitive marketplace.

In 1999, the FCC approved the Joint Board's recommendation for significant changes to the methodology used to compute high-cost support for *non-rural* carriers. The FCC adopted a mechanism that uses a forward-looking economic cost model to determine the support needed by carriers in high-cost states. The Joint Board and FCC are currently evaluating the needs of rural carriers, and reviewing the recent report of the Rural Task Force, with decisions to come in early- to mid-2001.

In addition to federal high cost support programs, the FCC has established a program for eligible schools and libraries to receive support for telecommunications services. The entities may obtain discounts on services, including Internet access and internal connections at discounts ranging from 20 to 90 percent. Another portion of the federal USF program provides support for rural health care providers to purchase telecommunications services at the same rates that health care providers in urban areas pay for those services.

Disbursements from the federal USF programs are shown in the following table.

Table A-2: Federal Universal Service Fund Program Disbursements to Texas Entities

Federal USF Program Disbursements	1998	1999
Total High Cost Support	$122,103,519	$119,556,528
Low Income Programs (Combined)	$19,868,956	$22,640,550
Schools & Libraries Funding	$129,802,468 (1/1/98-6/30/99)	$135,913,941 (7/1/99-6/30/00)
Rural Health Care Funding Commitments	$15,749 (1/1/98-6/30/99)	$35,068 (7/1/99-6/30/99)

Source: Universal Service Monitoring Report, CC Docket No. 98-202, Federal-State Joint Board on Universal Service, September 2000.

APPENDIX B: ACCESS CHARGES

In passing the Telecommunications Act of 1996 (FTA), Congress sought to establish "a pro-competitive, deregulatory national policy framework" for the United States telecommunications industry. In the FTA, Congress also directed that universal service support "should be explicit and sufficient to achieve the purposes" of section 254, which includes the purpose that all Americans should have access to telecommunications services at affordable and reasonably comparable rates. According to the FCC, implementation of the FTA required a trilogy of separate but related proceedings addressing regulatory reform in three important subjects: interconnection, universal service, and access charges. This appendix gives a brief overview of recent federal and state activity related to access charges. For additional information, the reader should refer to the *Report to the 77ᵗʰ Texas Legislature on Intrastate Switched Access Rates*, PUC Project No. 21168.

For much of this century, most telephone subscribers obtained both local and long-distance services from the same company, the pre-divestiture Bell System, owned and operated by AT&T. In the 1970s, MCI and other long distance carriers began to provide switched long-distance service in competition with AT&T. AT&T, however, still maintained monopolies in the local markets served by its local subsidiaries, the Bell Operating Companies (BOCs). The BOCs owned and operated the telephone wires that connected the customers in their local markets. Other independent (non-BOC) LECs held similar monopoly franchises in their local service areas. MCI and the other IXCs were dependent on the BOCs and the independent LECs to complete long-distance calls to the end user.

In 1983, following the decision to break up AT&T, the FCC adopted uniform rules governing the fees – the access charges – that long distance carriers should pay the local exchange carriers for originating and terminating interstate calls placed by or to end users on the local networks.

With the passage of the FTA, the FCC determined that it was necessary to make substantial revisions to access charges. In an attempt to more closely align the rate structure with the manner in which costs are incurred, the FCC initially shifted cost recovery from the carrier common line (CCL) access charge to the presubscribed interstate carrier charge (PICC), a flat per-line charge imposed by the local carrier on an end user's IXC. That plan was relatively short-lived, as customers were subjected to higher bills, and long distance charges were not reduced as much as expected.

According to the FCC, "[u]ndoing the Gordian knot of determining the appropriate level of interstate access charges and converting implicit subsidies in interstate access charges into explicit, portable, and sufficient universal service support cannot be accomplished with one stroke of the sword." After years of disputes and concerns over the structure and levels of access charges, the FCC adopted further modifications in May 2000, designed to balance various and sometimes conflicting interests – including promotion of competition, deregulation, maintaining affordability for all, and avoiding rate shock to consumers. The FCC adopted an integrated interstate access reform and universal service proposal for price-cap LECs put forth by the members of the Coalition for Affordable Local and Long Distance Service (CALLS). The CALLS proposal was designed to remove implicit subsidies from the interstate access charge system and replace them with a new interstate access universal service support mechanism that supplies portable support to competitors.

The FCC's *CALLS Order* combined two phone bill charges - the existing presubscribed interstate carrier charge and the subscriber line charge - into one line item. The FCC indicated that consumers would see savings through this plan, since long distance carriers committed to passing through access reductions to customers. As part of the plan, AT&T and Sprint agreed to eliminate from their basic rate plans the monthly minimum usage charges customers were paying whether or not they made any calls. The *CALLS Order* removed $650 million from access charges and replaced that revenue amount with a special "USF" assessment on all carriers' interstate revenues. The revenue from this assessment is available to any carrier serving customers in high-cost areas.

Texas' switched access rates were adjusted prior to 1999 in company-specific rate cases,[111] and in an industry-wide access reform rulemaking that eliminated the interexchange carrier access charge, shifting that revenue requirement to the CCL and other charges for individual local telephone companies.[112] Because the intrastate usage-based switched access rates were very high to begin with and no additional flat rate charge was employed, the significant reductions from these cases still leave intrastate switched access rates very high when compared to interstate rates.

Switched access rates have been significantly impacted in Texas during the last two years as a result of activities related to the Texas Universal Service Fund (TUSF) and PURA requirements. During the last half of 1999 and into the third quarter of 2000, the Commission made significant changes to the TUSF. In conjunction with PURA Section 58.301, the Commission implemented changes that substantially reduced the rates for switched access of a majority of the ILECS in Texas.[113] The PURA required Southwestern Bell Telephone Company to reduce its combined originating and terminating switched access charges by one cent per minute in September of 1999 and by an additional two cents per minute in July of 2000. This combination reduced the cost of switched access in SWBT territory by approximately twenty-five percent.

Additional access reform for Texas' intrastate switched access rates is described in greater detail in ***the Report to the 77th Texas Legislature on Intrastate Switched Access Rates.***

[111] Cases concluded in 1986 and 1990 for Southwestern Bell, and less frequently for other ILECs.

[112] Rulemaking Project No. 7205.

[113] As an example, SWBT's composite switched access rate went from approximately 12.2 cents to 6 cents per minute, for a reduction of over 50%. Appendix B provides a summary and comparison of the composite switched access rates for all of the states.

APPENDIX C: 9-1-1

The inability of wireless customers to benefit from the advanced emergency capabilities of enhanced 9-1-1 (E911) systems available to most wireline customers has been the predominant topic in the 9-1-1 industry in recent years. Most wireline phones are connected to E911 service that automatically reports the caller's location when 9-1-1 is dialed. On the other hand, when a 9-1-1 call is placed using a wireless handset, the dispatcher at the 9-1-1 Public Safety Answering Point (PSAP) does not know where the caller is. In 1996 the Federal Communications Commission (FCC) mandated the implementation and deployment of wireless enhanced 9-1-1 features and functions in two phases, to enable wireless callers to have the same benefits as wireline callers. Under Phase I, 9-1-1 systems must deliver the phone number of the handset from which an emergency call originates and the location of the base station carrying the call to the 9-1-1 operator. Under Phase II, 9-1-1 systems must locate handsets within a radius of 125 meters with a success rate of 67 percent. The requirements for Phase II do not take effect until Oct. 1, 2001.

The 76th Texas Legislature passed H.B. 1983, which gave the Commission on State Emergency Communications (CSEC) the responsibility for implementing wireless Phase I 9-1-1 services for at least 75% of the population served by the State program. This implementation was to be completed on or before August 31, 2000. The Commission worked closely with CSEC to help with deployment of Phase I in Texas. Specifically, the Commission worked with regulated carriers to ensure that trunks ordered by wireless carriers were installed and tested to meet the deadline set by H. B 1983. As a result, wireless Phase I 9-1-1 service was deployed in Texas covering 73.8% of the population served by the state program.

With the entrance of new competitors into the telecommunications market and the implementation of wireless Phase I service, the Commission has been faced with finding regulatory solutions to many other 9-1-1 issues. For example, the entrance of an alternative statewide 9-1-1-database provider has raised many issues, such as proprietary customer information being disclosed and 9-1-1 entities being able to buy network and database services from different vendors at reasonable prices. The Commission conducted a rulemaking and held many proceedings to ensure that the citizens of Texas will be protected through a 9-1-1 network that works efficiently and effectively in a competitive telecommunications market. As a result the Commission adopted P.U.C. SUBST. R. § 26.433, relating to the Roles and Responsibilities of 9-1-1 Service Providers. This rule establishes specific reporting and notification requirements and mandates certain standards for network interoperability, service quality, and database integrity. These requirements are in addition to the minimum interconnection parameters for E911 contained in P.U.C. SUBST. R. § 26.272.

As a result of proceedings and rulemakings over the last year, Texas citizens should benefit from improvements in 9-1-1 service while using cellular phones. Still, much more work needs to be done to ensure the reliability of the state's emergency 9-1-1 system in a competitive telecommunications environment. The Commission is currently conducting proceedings to approve E911 tariffs filed by Southwestern Bell Telephone Company (SWBT) and Verizon Communications (formerly known as GTE Southwest, Inc.). The Commission is currently conducting proceedings to approve E911 tariffs filed by SWBT and Verizon Communications.

APPENDIX D: PAY TELEPHONES

To promote further competition in the payphone industry, the FCC in 1996 deregulated coin rates for all local calls made from payphones. That same year the PUC began to register and certify payphone service providers, as required by the revisions to PURA in 1995. Pay Telephone Rules were reviewed and readopted pursuant to the Government Code Procedures Act. Revision of P.U.C. SUBST. R. § 23.54 incorporated the Commission's authority, granted under Senate Bill 86, to revoke a provider's certificate for violation of Commission's rules and carry out the sunset review process.[114]

Data show that local telephone companies have been reducing their involvement in the payphone business. The number of payphones that ILECs provided declined from 90,200 in 1998 to 86,400 in 1999, while the number of lines provided to competitive payphone providers fell from 56,300 in 1998 to 46,500 in 1999.

Table 28 – Pay Telephones in Texas

	1998	1999
Number of payphones provided by incumbent local telephone companies:	90,193	86,404
Number of loops provided by local telephone companies to competitive payphone providers:	56,316	46,492
Total number of payphones:	146,509	132,896
Payphones provided by competitive payphone providers, as percent of total payphones:	38.4%	35.0%

Source: Public Utility Commission of Texas Data Request

[114] To implement these provisions of SB 86, the Commission adopted P.U.C. SUBST. R. 26.102 *Registration of Pay Telephone Service Providers;* P.U.C. SUBST. R 26.341 *General Information Relating to Pay Telephone Service (PTS);* P.U.C. SUBST. R 26.342 *Pay Telephone Service Tariff Provisions;* P.U.C. SUBST. R 26.343 *Pay Telephone Service of Certificated Telephone Utilities holding Certificates of Convenience and Necessity;* § 26.344 *Pay Telephone Service Requirements;* § 26.345 *Posting Requirements for Pay Telephone Service Providers;* § 26.346 *Rates and Charges for Payphone Service;* and P.U.C. SUBST. R 26.347 *Relating to Fraud Protection for Pay Telephone Service.*

APPENDIX E: NUMBERING ISSUES

AREA CODE ACTIVITY

During this reporting period (January 1999 – December 2000), the Commission has seen several changes in area code activity. The primary reason for the recent changes has been a drastic increase in technology that utilizes numbers. Pagers, faxes, personal and multiple telephone lines have all contributed to a sharp growth in the number of central office 3-digit prefixes (NXX codes) needed by carriers. As Table 29 illustrates, the boom in area code growth in Texas has occurred mostly over the previous five years.

The Commission has reacted to the exhaustion of area codes by splitting area codes or overlaying one area code with another. Splitting an area code simply requires breaking up a full area code into two or three smaller codes, with one area keeping the original code and new area code(s) being assigned to the other area(s). An overlay entails the assignment of a new area code over the same geographical area as the current code. The outcome of an overlay is ten-digit dialing, that is, customers must dial the area code and the seven-digit number for all local calls. Toll, or long distance, calls are then made by dialing a "1" before the area code and phone number.

Table 29 – Texas Area Code Chronology

1947	**4 area codes** 214 – Northeast Texas 512 – Central and South Texas 713 – Southeast Texas 915 – West Texas
1953	**5 area codes** 817 – a geographic split of the Fort Worth region from 214
1962	**6 area codes** 806 – a geographic split of the Amarillo/Lubbock region from 915
1983	**7 area codes** 409 – a geographic split from 713
1990	**8 area codes** 903 – a geographic split of the Longview region from 214
1992	**9 area codes** 210 – a geographic split of San Antonio from 512
1996	**11 area codes** 972 – a geographic split of the 214 area code serving the Dallas region 281 – a geographic split of the 713 area code serving the Houston region
1997	**15 area codes** 254 and 940 – a three-way geographic split of 817 830 and 956 – a three-way split of 210 with San Antonio retaining that area code
1998	**15 area codes** The geographic boundary between 214 and 972 in Dallas is erased, creating the first overlay in Texas. Ten-digit dialing is required for local calls.
1999	**18 area codes** The geographic boundary between 713 and 281 in Houston is erased, creating an overlay and requiring ten-digit dialing for local calls. 831 – an overlay added as the third Houston area code 361 – a geographic split of 512 creates a new area code for the Corpus Christi region 469 – an overlay added as the third Dallas area code
2000	**21 area codes** 979 and 936 - a three-way split of 409 with Beaumont retaining that area code 682 – an overlay added to 817 for Fort Worth and part of Northeast Texas

Source: Public Utility Commission of Texas

The following is a summary of the major actions taken by this Commission with respect to the area codes in Texas.

- **214, 469, and 972:** On December 5, 1998, mandatory ten-digit dialing for both the 214 and 972 area codes began. These area codes began as a concentrated overlay and, in December, the split between the two codes was eliminated, creating a single area served by the 214 and 972 area codes. Due to high demand for numbers in the Dallas metropolitan area, on July 1, 1999, a third area code, 469, was introduced to cover the same area as 214 and 972.
- **281, 713, and 832:** Area code relief in the Houston metropolitan area was along the same lines as that in the Dallas area described above. On January 16, 1999, the split between 281 and 713 was eliminated, and a new area code, 832, was introduced to cover the same area as 713 and 281.
- **409, 936, and 979**: To delay the need for an overlay and ten-digit dialing, on October 13, 1999, the Commission approved a three-way geographic split

of the 409 area code. Beaumont, Galveston, Port Arthur and Texas City retained the 409 area code. Conroe, Huntsville, Lufkin, and Nacogdoches took the new 936 area code, and 979 was assigned to Bay City, Brenham, Bryan, College Station and Lake Jackson. As of August 5, 2000, new area code usage became mandatory.

- **361 and 512:** Due to the amazing rate of growth in this area code, on October 16, 1999, the Corpus Christi area was split from the 512 area code and was assigned the new area code of 361. Thereafter, even though the 512 area code encompassed mostly the Austin metro area, it again quickly approached a jeopardy situation and was slated for exhaust in the third quarter of 2003. To extend the life of the 512 area code, on March 29, 2000, the Commission issued an order implementing thousand block number pooling in the 512 area code. Simultaneously, to comply with an FCC order, the Commission issued an order adopting a relief plan consisting of a concentrated overlay along the Interstate-35 corridor. This overlay will encompass mostly Austin, Georgetown and San Marcos. Although the overlay is tentatively scheduled for August 4, 2001, the Commission's order requires Commission Staff to evaluate the impact of number pooling and report to the Commission by June 1, 2000, for the express purpose of determining whether the overlay needs to actually be implemented in August 2001 or whether it can be further delayed. As discussed below, the impacts of number pooling have been extremely positive, and the life of the 512 area code has been extended significantly.
- **682 and 817:** As of December 1999, the Commission approved an overlay for the 817 area code, which covers the Fort Worth area. Beginning on October 7, 2000 cities such as Arlington, Euless, Fort Worth, and Glendale were required to use ten-digit dialing for local calls. The new area code, 682, overlays the entire geographical area covered by the 817 area code.
- **903:** Although 903 has not been declared in jeopardy, it is projected to exhaust sometime in the fourth quarter of 2002. Consequently, the Commission and the industry have begun exploring options for this far-northeast Texas area code.
- **210, 915:** These area codes in San Antonio and West Texas are both codes that the Commission is beginning to monitor closely as they approach their projected exhaust dates.

In addition to specific customer education for each change in area codes, the Commission maintains an area code website that tracks activity statewide. The website also includes a listing of NXXs (also known as prefixes) by city.

N11 Codes

Another development in the world of numbering has been the increased use of FCC administered N11 codes. The federal government recognizes only 211, 311, 511, and 711 as nationally assigned NXXs. However, other codes have traditional uses, as shown below.

N11 Code	Description
211	Community Information and Referral Services (US)
311	Non-Emergency Police and Other Governmental Services (US)
411	Local Directory Assistance
511	Traffic and Transportation Information (US); Reserved (Canada)
611	Repair Service
711	Telecommunications Relay Service (TRS)
811	Telephone Companies' Business Offices
911	Emergency

The FCC does not direct state commissions to administer the N11 codes. Further, there really are no concrete industry guidelines for the assignment of N1 codes; interested parties generally just contact the North American Numbering Plan Administrator (NANPA). However, because the codes affect locally run services, they are important to the citizens of Texas. Examples of local areas utilizing available codes are the recent actions of Dallas and Austin to begin using the 311 code for city-administered maintenance, repair, and other non-emergency services.

Recognizing the importance of N11 codes, on October 20, 2000, the Texas Commission proposed to amend its P.U.C. SUBST. R. §26.127, relating to ***Abbreviated Dialing Codes***, to designate the 211 code for community services information and 511 for traffic and transportation information. The 211 dialing code was requested by the Texas Health and Human Services Commission to implement the establishment of a statewide clearinghouse number for community services and will provide free information and referrals to community resources. Assignment of 211 for this purpose is expected to alleviate some of the congestion on the 911 network and to aid the state network of health and human services in coordination. The FCC assigned 211 for community information and referral services on July 21, 2000, at which time it also assigned 511 for traffic and transportation information.[115]

The Commission has encouraged the utilization of the 711 code for Telecommunications Relay Service ahead of the federal implementation mandated date of October 2001. As of October 2000, the 711 code was available in most parts of Texas that were not served by SWBT, which will deploy the code by the end of February 2001. Formal proceedings by the Commission were not necessary because it negotiated with the Texas Telephone Association to take the initiative to start 711 throughout the state without any substantive rule forcing action. The Commission will contract out an outreach project to educate companies and agencies providing PBX systems that need to be modified and to work with payphone service companies and wireless providers that have not complied by the time SWBT deployment is completed.

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[115] Third Report and Order and Order on Reconsideration (FCC 00-256/FCC 00-257) (Order). The Texas Commission will hold a public hearing to discuss the implications of these new dialing codes at the Commission on January 9, 2001.